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COMMENTS ON TOPIC TWO: \*TRENDS IN ECONOMIC DEVELOPMENT AND IMPL--ETC(U)  
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April 1981

Comments on Topic Two: "Trends in Economic Development and Implications for Stability." by David Dapice, Tufts University

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Dr. Gillis has written a useful paper, pointing out that getting an acceptable magnitude and structure of growth with equity in an oil rich country is difficult. My comments will not be so much critical of his paper as complimentary.

Let us think about Indonesia's history for a moment. The Dutch ruled for several centuries by coopting and repressing dissidents, emphasizing ethnic differences, and denying education to almost everyone. The economy suffered badly in the 1930's and was drained by World War II and the subsequent revolution. The new nation faced a period of sustained instability in the 1950's and 1960's marked by corrupt parliamentary governments, religious and regional rebellions, hyperinflation, foreign adventurism, and violent political conflict. The nation also started its existence with a pitifully small human resource base. In 1961, four out of five men and nine out of ten women had zero to five years of schooling. There were then only twenty thousand university graduates in a country of nearly 100 million. The real value of civil servants' pay, and of other government spending, was cut sharply during the middle 1960's. The economy was then stagnant or declining, and consumption of food was falling to dangerously low levels.

The last fifteen years have seen a marked turnaround in the general economic situation. Real per capita income has doubled. There have been windfalls from oil, timber, foreign aid, and private investment. Much of these funds have been and are being misused, with no necessary trend towards improvement. However, it would be obfuscatory to deny the progress taking place. In 20 years the fraction of children in primary school has risen from 3/5 to 9/10; with even faster rates of growth (from lower starting and ending levels) for secondary schools. There were over 300,000 university students in 1978, up from 87 thousand fifteen years prior. There have also been improvements in infant mortality, food production and - more recently - food consumption per capita, as well as some progress in family planning. Further gains are likely, but will fall well short of what could be done if resources were better used, or what will be needed to reduce the poverty of large fractions of the population.

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There have grown up in the last decade or so significant vested interests. They have a large stake in maintaining the present system which channels government support\* in large amounts to relatively few and modest amounts to a significant minority. This group is somewhat worried about foreign (e.g. Vietnamese) support or extreme Islamic movements linking up with domestic discontent. They dislike "excessive" internal criticism. But they are, I suspect, fairly confident in their ability to buy off or repress opponents, and otherwise control events. (Although the recent move to stop all TV ads suggests that too rapid rising expectations are also of concern.)

It is in this general context that we should consider the medium to long run task of economic development. It is likely that the importance of net oil/gas exports, and tax revenues, will fall over the next decade or two, almost certainly relative to GNP and quite possible in absolute (real) terms. Severe problems of employment and income distribution could be ameliorated now, and longer run structural adjustments would be eased, if a large segment of industry were labor intensive, competitive, and able to respond to new opportunities. One might add that the pribumi would have to play a large role in this industrial growth. Hand in hand, agriculture would have to increase productivity per unit of land, improve irrigation, tree crops yields, and upland cropping patterns. These changes require relatively undistorted prices (including petroleum prices), a fair degree of administrative capability, and a mechanism to control corruption.

The outlook is mixed. Devaluation in 1978 has helped labor intensive activities, and fuel prices have been raised twice in three years by 50% each time. But the likelihood is that within a few years a devaluation would again be needed to correct the effects of inflation above world levels, and fuel prices are still very heavily subsidized. (Diesel oil is selling at 25¢ per gallon!) Both might prove difficult to change very much if there is no short run reason to do so. Credit is hard to get, often too low in price, and still too unlikely to be repaid. There are significant distortions in tariff levels. Aid to pribumi is frequently ineffective and politically guided. Corruption was, is, and is likely to remain a significant impediment to imple-

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\* Government support means access to resources beyond general spending on health, education, roads, etc.

mentation of decentralized programs aimed at reaching groups with low productivity. The private sector is relatively weak, with limited political influence.

Against this list of negatives are some positives. An impressive capability exists within BIMAS and BULOG to grow, buy, store, and sell rice. If this capability is extended to other crops, and if irrigation investments continue at high levels, the outlook for food production and perhaps farm employment is good. The industrial base is both deeper and wider than it was, and there is a growing (though still modest) entrepreneurial group with proven experience. The government seems willing to put money into these areas. Exports of manufactured goods are growing, real wages have not been rising, and prices have been rising at only British levels (1979 IV - 1980 IV) after a 50% devaluation. If the world economy does not contract sharply in terms of market opportunities, if costs in Indonesia do not rise too quickly, and if administrative controls on these exports can be minimized, a considerable amount of employment could result.

What signs will there be of success in dealing with these dilemmas? A suggestive list follows:

In energy - a program to reduce gradually petroleum subsidies and investments to diversify the sources of energy consumption.

In industrial employment - continued efforts to maintain domestic costs at reasonable levels vis a vis competitors, reduce administrative interference, and provide effective assistance via credit and technical assistance.

In agriculture - a mixed strategy of increasing productivity by greater irrigation and intensified rainfed agriculture, new areas brought into cultivation in the Outer Islands, and better tree crop productivity. Mechanization policies will have to be deliberate and restrained.

In corruption - some efforts to contain its effects, which are extreme tendencies towards capital intensity, inefficient implementation of decentralized programs, and further concentration of income. Allowing freer press coverage, collection of significant income and real estate taxes, and restraint at the higher echelons would all be good signs.

In monetary/fiscal policies - a combination of effective surpluses in the government budget, slower rates of monetary expansion (e.g. 20% - 25% instead of 40%) and adequate provision for credit expansion in the private sector.

Improvements in banking practices, collections, and credit access would help a lot.

Whatever the outcome of the deliberations on these issues, it is not likely that foreigners will have very much leverage on decision making in the near future. With ten billion dollars in foreign reserves, stable rice prices and high rice stocks, and more attention to internal than external developments, few of the elite in Indonesia wish to be lectured or threatened. With some luck, they can be reasoned with. Their slightly longer run self-interest surely lies in programs that require moderate short run sacrifices or restraint. If this premise were accepted, the outlook could be reasonably good.

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